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IN THE

**Supreme Court of the United States**  
OCTOBER TERM, 1989

MICHAEL J. CONNOLLY,  
Massachusetts Secretary of State,  
and  
BARRY C. GUTHARY, Director,  
Massachusetts Securities Division,  
*Petitioners,*

v.

SECURITIES INDUSTRY ASSOCIATION, et al.,  
*Respondents.*

*Petition for Writ of Certiorari to  
the United States Court of Appeals  
for the First Circuit*

**BRIEF FOR NORTH AMERICAN  
SECURITIES ADMINISTRATORS  
ASSOCIATION, INC.,  
AS AMICUS CURIAE**

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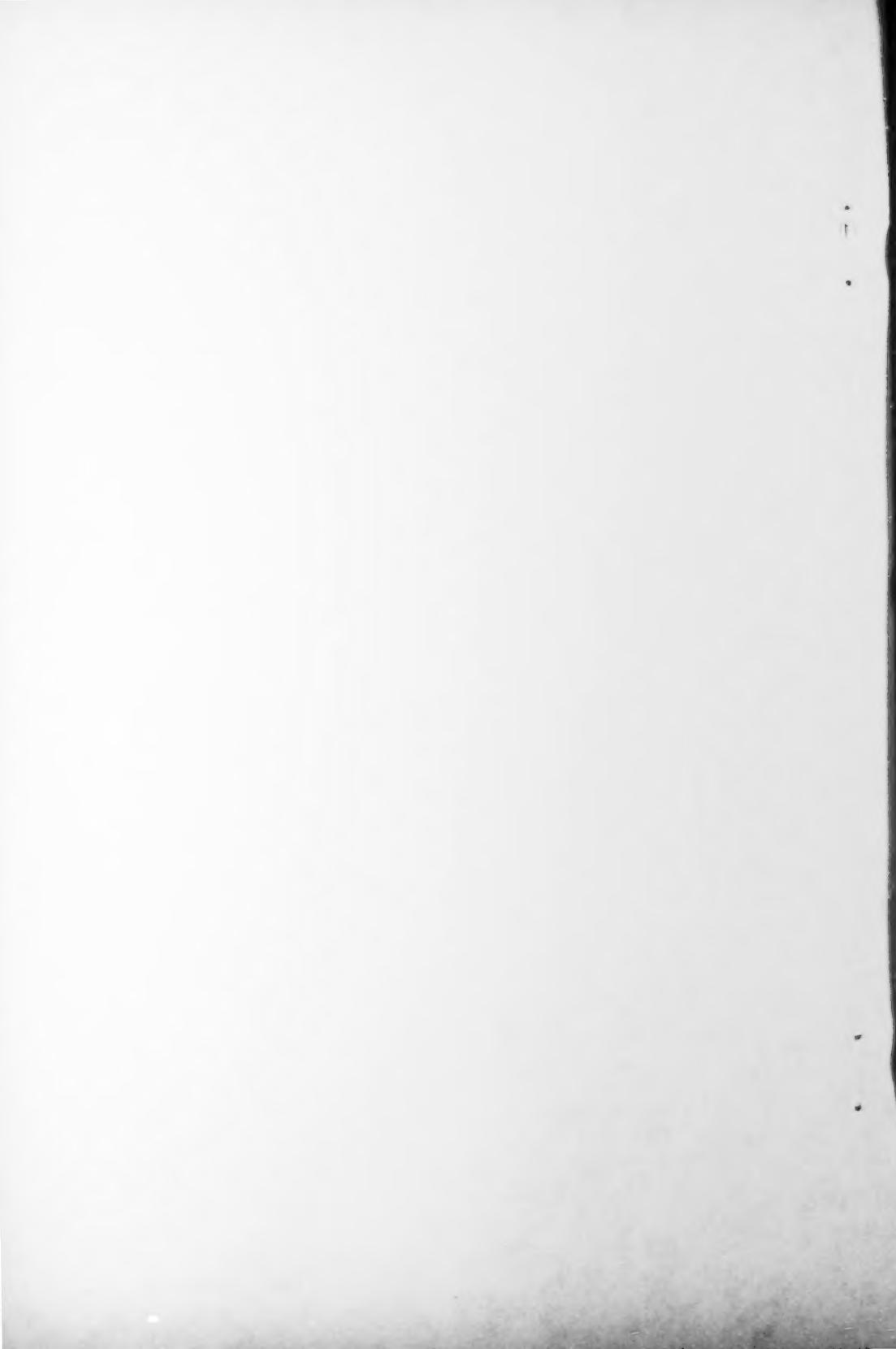
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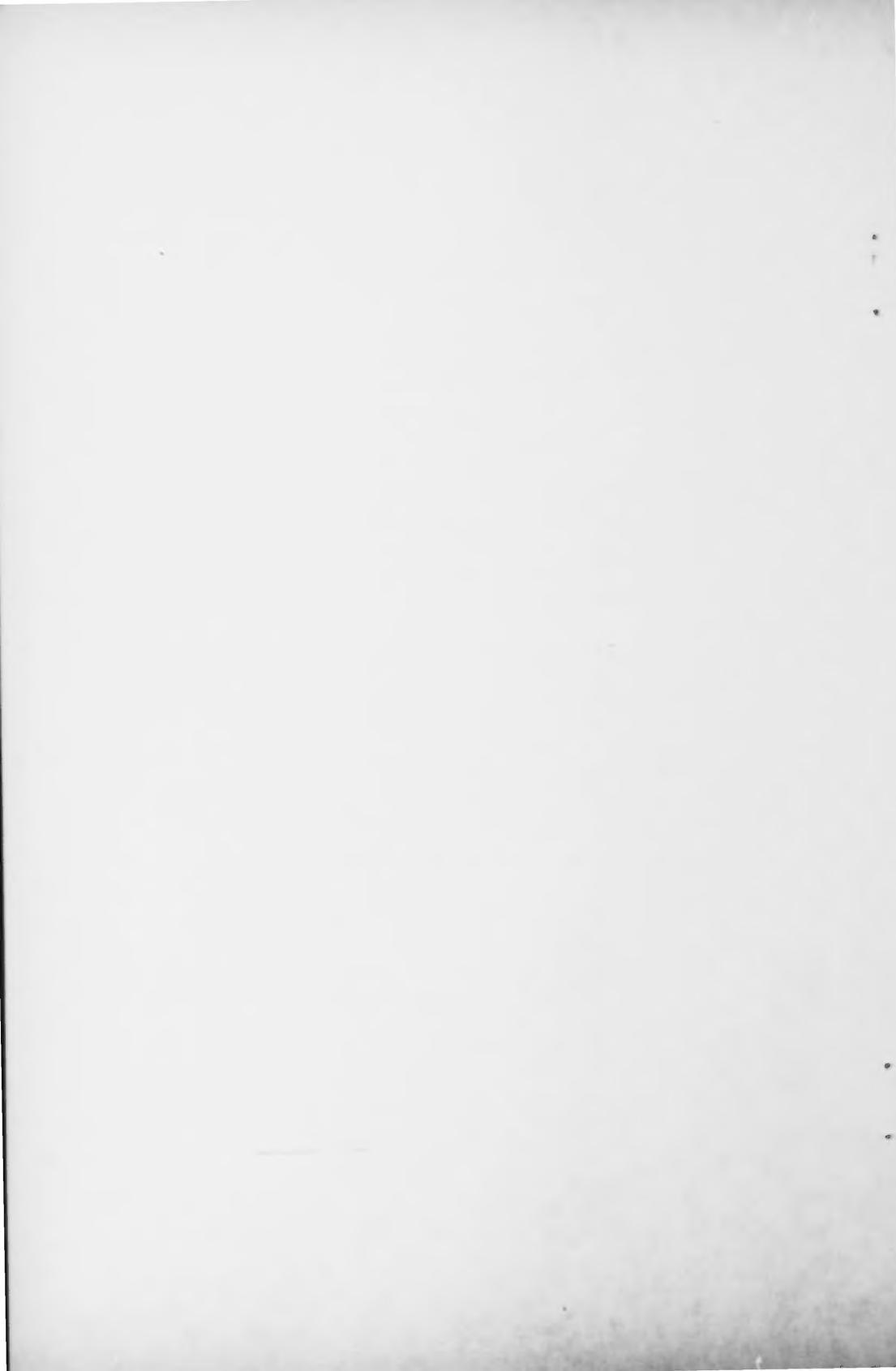
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**AUTHORITY TO FILE AND POSITION  
OF AMICUS CURIAE**

This brief is filed pursuant to Rule 36.1 of the Court's Rules by written permission of the parties to the case. Such written permission is filed herewith. The brief supports the position of the petitioners.



STATEMENT OF THE INTEREST  
OF THE AMICUS CURIAE

The North American Securities Administrators Association, Inc. ("NASAA") is an association of state and provincial securities administrators in the United States, including the District of Columbia and Puerto Rico, Canada and Mexico, which, since 1918, has worked for investor protection. State securities commissioners are charged with regulating the securities markets and combatting securities frauds in their respective jurisdictions.

The dual system of federal and state regulation of securities is recognized by Section 18 of the Securities Act of 1933, 15 U.S.C. § 77r, and Section 28 of the Securities Exchange Act of 1934, 15 U.S.C. § 78bb, which reserve jurisdiction of state securities commissioners over any security or person. Through this dual



system, the coordinated enforcement efforts of NASAA and the Securities and Exchange Commission ("SEC") have resulted in a most effective system for the enforcement of the securities laws. The SEC concentrates in large scale enforcement actions on international or multi-state levels, with the state commissioners either serving in a back-up or assisting role in such large scale actions or concentration on more local or regional enforcement actions.

The interest of NASAA in the present case is three fold. First, the Massachusetts Division of Securities, a NASAA member, has asked NASAA to participate in the present proceedings and to file an amicus curiae brief because of the impact that the decisions below will have upon the regulations he adopted and the Act that he administers. NASAA has already participated in the proceedings



before the Securities Division by having its General Counsel, Lee Polson testify. See Record Before the Secretary at 30-50; 104-176. It also filed an amicus curiae brief with the First Circuit.

Second, many other NASAA member agencies or states would like to consider adopting statutes or rules similar to the one adopted by the Massachusetts Division in the present case. In September 1988, NASAA released a report which indicated that fifteen of its member agencies were considering rules similar to that adopted by the Massachusetts Division. Among these states were: Florida, Georgia, Idaho, Iowa, North Dakota, Ohio, Pennsylvania, South Dakota, Washington, and Wisconsin. 20 Sec. Reg. & L. Rep. (BNA) 1436 (Sept. 23, 1988). In addition bills have been introduced in the legislatures of five states, California, Louisiana, Maryland, Oregon, and



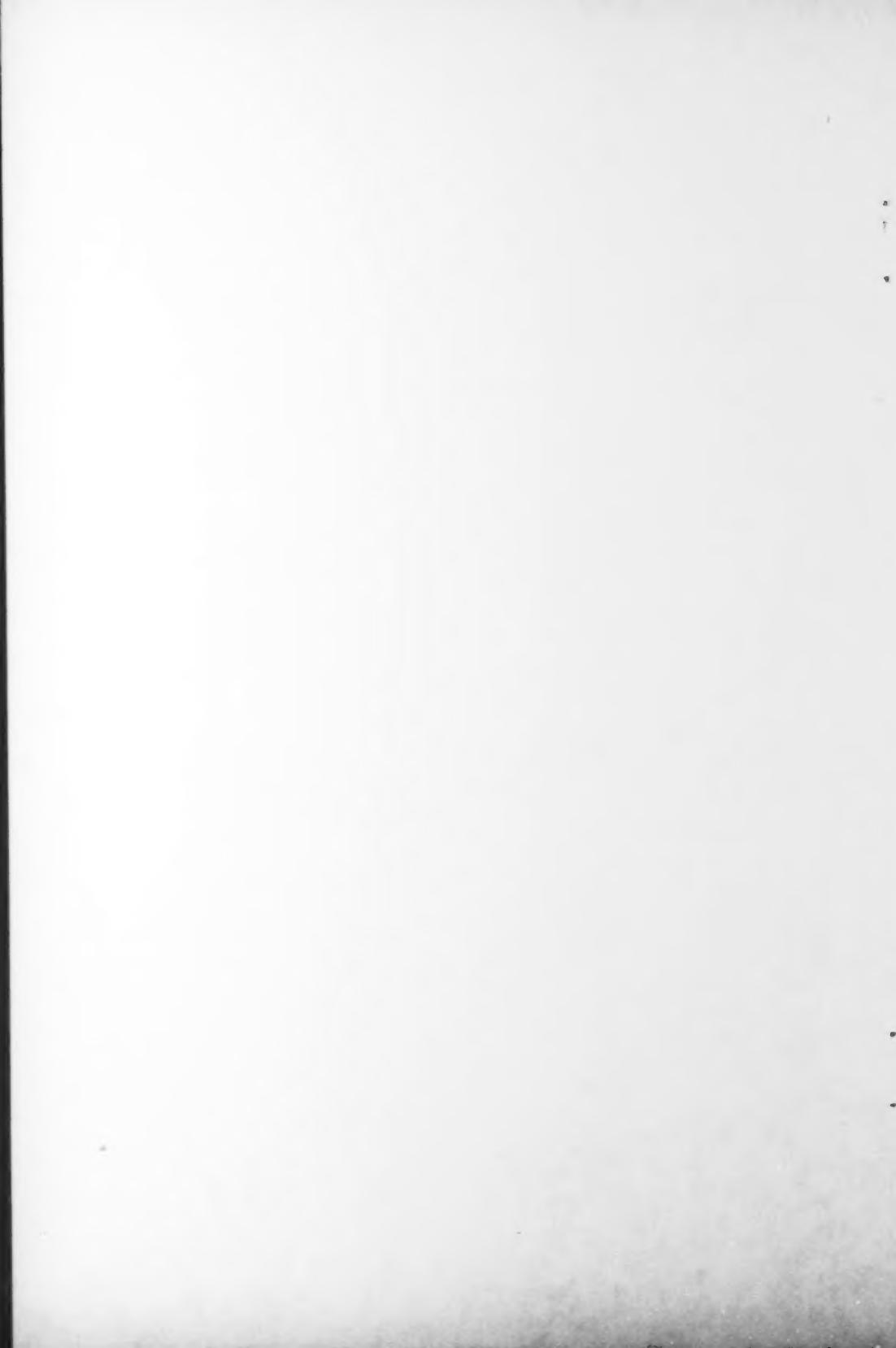
Washington, to bar broker-dealers from requiring mandatory arbitration clauses in their brokerage contracts as a condition for opening an account. See Cal. SB No. 1889, discussed in 20 Sec. Reg. & L. Rep. (BNA) 381 (Mar. 11, 1988); La. SB No. 74, discussed in 21 Sec. Reg. & L. Rep. (BNA) 745 (May 19, 1989); Md. SB No. 72, discussed in 21 Sec. Reg. & L. Rep. (BNA) 82 (Jan 13, 1989); Ore. SB No. 925, discussed in 21 Sec. Reg. & L. Rep. (BNA) 1805 (Dec. 8, 1989); Wash. SB No. 5787, discussed in 21 Sec. Reg. & L. Rep. (BNA) 980 (July 7, 1989).

Since the decision by the First Circuit in the present case, an informal survey of its member agencies by NASAA shows that three members, Delaware, North Carolina, and Iowa, have plans to consider rules similar to the Massachusetts rule in 1990. In addition, the Oregon legislature has established an interim legislative



committee to consider mandatory arbitration clauses with a view toward introducing bar legislation in the 1991 session. 21 Sec. Reg. & L. Rep. (BNA) 1805 (Dec. 8, 1989).

Finally, NASAA, as an organization, is extremely interested in ensuring that the investors are treated in a fair and unbiased manner in the arbitration process. This concern has lead NASAA to call continually for federal and state regulation to ensure the voluntariness of arbitration agreements. In September 1987, immediately following this Court's decision in Shearson/American Express, Inc. v. McMahon, 482 U.S. 220 (1987), NASAA formed an Ad Hoc Committee to study arbitration and to make recommendations how the process could be improved to provide greater investor protection. In December 1987, NASAA urged Congress to require brokers to negotiate arbitration



agreements and to provide potential customers with a separate disclosure document which would explain the terms and implications of mandatory arbitration clauses. Statement of James C. Meyer Before the Subcomm. on Telecommunications and Finance of the House Comm. on Energy and Commerce (Dec. 16, 1987). NASAA's concern were noted in the comments of Subcommittee Chairman Markey and member Boucher and several witnesses at a hearing before this same subcommittee on March 31, 1988. 20 Sec. Reg. & L. Rep. (BNA) 492 (Apr. 1, 1988). On June 1, 1988, NASAA's Ad Hoc Committee published its recommendations for a "top-to-bottom overhaul" of the securities arbitration procedures including a prohibition on broker-dealers denying services to customer who refuse to sign predispute arbitration agreements. 20 Sec. Reg. & L. Rep. 850 (June 3, 1988). A week later,



NASAA's president James Meyer, Director of the Tennessee Division of Securities, appeared before the House Energy Subcommittee and again urged Congress to prohibit broker-dealers from demanding the signing of predispute arbitration agreements as a condition for opening a brokerage account. 20 Sec. Reg. & L. Rep. (BNA) 870 (June 10, 1988). This testimony lead, in part, to the introduction by Representative Boucher of HR 4960, 100th Cong. 2d Sess., on June 30, 1988, which included a provision barring arbitration clauses as a precondition for opening a securities account. 20 Sec. Reg. & L. Rep. (BNA) 1054 (July 8, 1988).

REASONS FOR GRANTING THE WRIT

A year ago this case would have come to the Court by appeal as a matter of right under former 28 U.S.C. §1254(2). Cf. City of New Orleans v. Dukes, 427 U.S. 297 (1976). Today the case comes before the



Court under the discretionary writ of certiorari. As will be seen below, the outcome should not change. The Court should grant full review because the case meets the Court's traditional test for the granting of certiorari formulated by Chief Justice Taft that it "involve[s] principles, the application of which are of wide public importance or governmental interest, and which should be authoritatively declared by the final court." Stern, Gressman, and Shapiro, Epitaph for Mandatory Jurisdiction, 74 ABA J. 66, 68 (Dec. 1988). The case also meets other often-cited tests for the granting of certiorari in that there is a potential conflict between the Circuits and that the lower courts made a major mistake in the interpretation of the relevant federal statute which will have wide impact. Each of these points will be examined below.



I. THE DECISION BELOW PRESENTS AN IMPORTANT QUESTION CONCERNING THE PREEMPTION OF THE STATE'S AUTHORITY TO PROTECT INVESTORS IN THE FORMATION OF ARBITRATION AGREEMENTS.

The case involves a Rule adopted by the Massachusetts Securities Division under the Massachusetts Uniform Securities Act. The Rule declared, among other things, that it was an unethical business practice for a broker-dealer to demand that a customer sign a predispute mandatory arbitration clause as a condition for the opening of a brokerage account. The Rule also required the broker-dealer to disclose the legal effect of such predispute arbitration agreements. The Rule did not prohibit predispute arbitration clauses. Instead it required two things: (1) that such clauses be the product of negotiation between the parties, and voluntarily accepted by the brokerage customer, rather than being a



contract of adhesion imposed upon the customer by the broker as a condition of doing business; and, (2) that the customer be given information about the effect of such agreement so that he could make an intelligent choice as to whether he wished to accept it. Such Rule is clearly within the police power of the Commonwealth. Hall v. Geiger-Jones, 242 U.S. 539 (1917). The First Circuit, however, held that the Rule was implied pre-empted because it conflicted with the Congressional policy behind the Federal Arbitration Act, 9 U.S.C. §1 et seq.

Because of the delicate balance between the dual sovereigns within our Federal system, this Court, on a number of occasions, has indicated that federal preemption should be cautiously approached when a federal-state balancing of respective governmental powers between the two sovereignties is involved. Jones



v. Rath Packing Co., 430 U.S. 519 (1977); United States v. Bass, 404 U.S. 336 (1971); Florida Lime & Avocado Growers, Inc. v. Paul, 373 U.S. 132 (1963); Rice v. Santa Fe Elevator Corp., 331 U.S. 218 (1947). Thus preemption "is not to be lightly presumed". California Federal Savings & Loan Ass'n v. Guerra, 479 U.S. 272, 281 (1987); Maryland v. Louisiana, 451 U.S. 725, 746 (1981). This is particularly true where the claim to preemption is implied rather than express, Aloha Airlines v. Director of Taxation, 464 U.S. 7 (1983), and where the field claimed to be preempted is one within the traditional police power of the state. Hillsborough County v. Automated Medical Inc., 471 U.S. 707, 715 (1985); Jones v. Rath Packing Co., supra. As a result this Court has stated: "We start with the assumption that the historic police powers of the State were not to be superseded by



the Federal Act unless that was the clear and manifest purpose of Congress." Rice v. Santa Fe Elevator, supra, at 230.

Because of the delicate balance between federal government as the superior sovereign and Commonwealth of Massachusetts as the inferior sovereign in the present case, the extreme caution which this Court has indicated should be exercised when implied rather than express preemption is involved, and the presumption against such preemption in areas traditional within the police power of the states, the Commonwealth of Massachusetts has a right to expect that the final decision on preemption of the Rule adopted by its Securities Division will be made by this Court rather than some inferior federal court. In the words of Chief Justice Taft, this is a case which "involves principles, the application of which are of wide

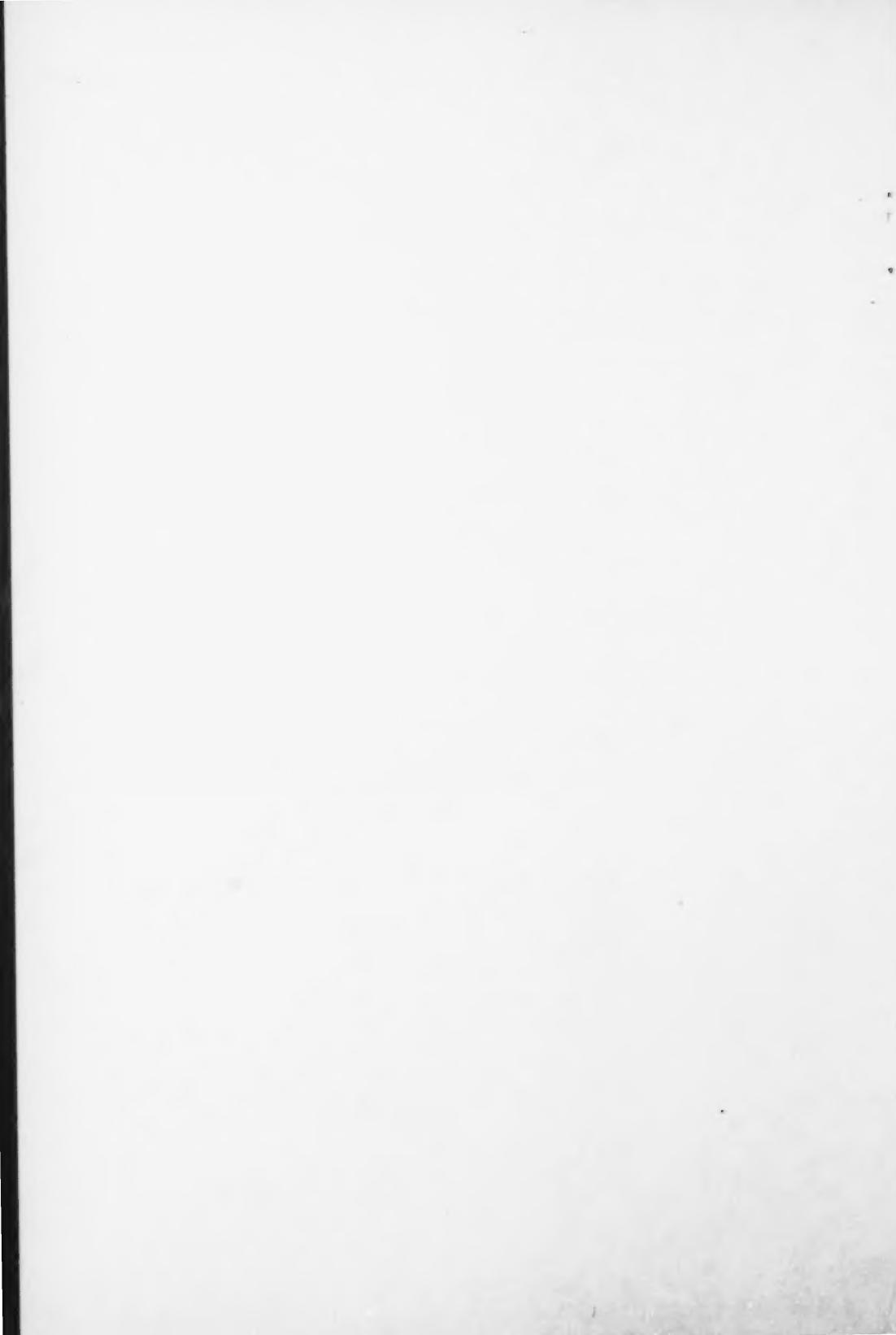


...governmental interest, and which should be authoritatively declared by the final court." While the right of the Commonwealth to demand such hearing ended with the repeal of Section 1254(2), this Court should exercise its discretion, grant review by certiorari, and definitively determine whether the Massachusetts Rule is implied preempted by the Federal Arbitration Act.

II. THE COURT SHOULD GRANT CERTIORARI BECAUSE THE CASE HAS NATIONAL INTEREST TO ALL SECURITIES REGULATORS.

The second part of Chief Justice Taft's test for the granting of certiorari is that the case has national significance and be one which should be authoritatively settled by the final court. Again the present case meets these criteria.

NASAA and its member state agencies have been increasingly concerned that mandatory ~~med~~dispute arbitration clauses



are becoming contracts of adhesion. As such, the individual investor has little or no choice as to whether he wishes to accept such an agreement. If he wishes to participate in the public securities market utilizing the services of a broker-dealer, he must agree to such a provision. As will be seen below, this is clearly contrary to the intent of Congress in adopting the Federal Arbitration Act.

Congress intended to make sure that a contract to arbitrate voluntarily agreed to by the parties would be enforced according to their agreement. Volt Information Sciences, Inc. v. Board of Trustees of Leland Stanford Junior University, \_\_\_ U.S. \_\_\_, 109 S.Ct. 1248 (1989). It clearly did not intend to force persons to arbitrate when there was no voluntary agreement to do so. A contract of adhesion requiring a mandatory predispute agreement to arbitrate where



the individual investor has no choice, but to accept or refrain from participating in the market, is not a voluntary agreement. This is especially true when viewed in light of the fact that the regulations of the New York and American Stock Exchanges and the National Association of Securities Dealers require all their members to arbitrate claims with their customers, if the customer so requests.

The industry's own statistics bear out that the mandatory arbitration clause is rapidly becoming a contract of adhesion. The industry figures reported to the Securities and Exchange Commission indicate that a year after this Court's decision in Shearson/American Express, Inc. v. McMahon, supra, in June 1988, that members of the brokerage community required a mandatory arbitration clause in 90 percent of their margin accounts and in 95 percent of their option accounts. 20



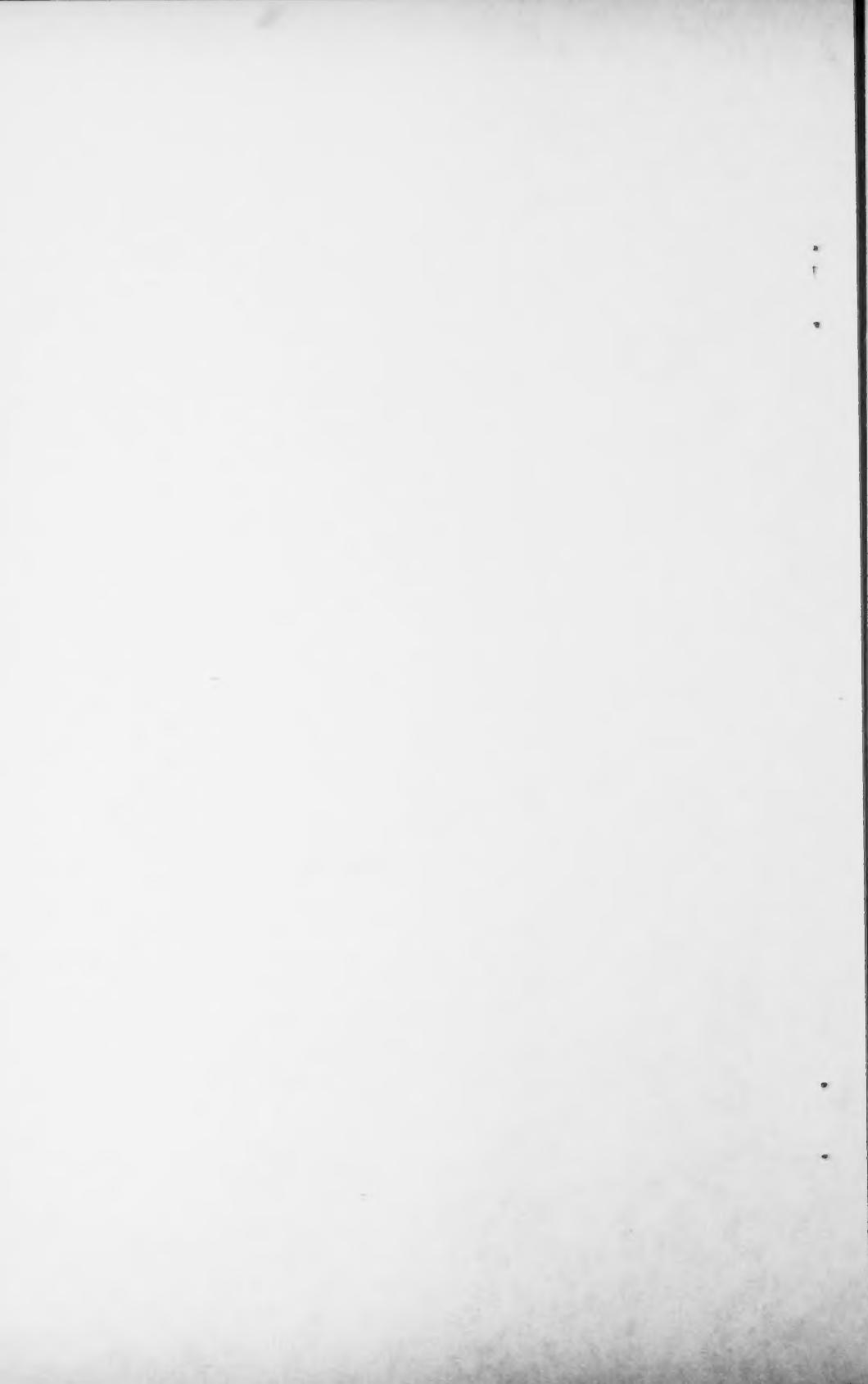
Sec. Reg. & L. Rep. (BNA) 833 (June 3, 1988). This percentage will become even greater as a result of the adoption by the Securities Industry Association of its new Model Customer Agreement form on July 17, 1989. This form contains a mandatory arbitration agreement for all margin customers. SIA has recommended that all its member firms adopt the Model Agreement form. 21 Sec. Reg. & L. Rep. (BNA) 1103 (July 8, 1989).

Industry spokesmen point out, however, that such mandatory agreements are required in less than 50 percent of the industry's cash accounts. This figure, while accurate at the time it was made, is now misleading for several reasons. First, many of the people who have cash accounts also have margin or option agreements, whether or not they actually trade on margin or in options. Typically, such margin or option agreements require the



arbitration of all disputes with the broker whether they arise out of a margin or option transaction or not. As a result, a very large number of cash account disputes are covered. It is only the cash customer who does not execute a margin or option agreement who will avoid the broker's mandatory agreement.

Second, both the industry spokesmen and the SEC Staff admit that the practice of requiring mandatory arbitration clauses in cash accounts is increasing. Three months after the McMahon decision, in September 1987, industry official predicted that companies will be encouraged by their own legal advisers to have cash customers sign predispute arbitration agreements. 19 Sec. Reg. & L. Rep. (BNA) 1388 (Sept. 18, 1987). This trend was confirmed by the SEC Staff in June 1988 when the Director of Market Regulation reported that there was a growing broad based trend toward



requiring predispute arbitration agreements in cash accounts. 20 Sec. Reg. & L. Rep. (BNA) 833 (June 3, 1988).

Recognizing this growing trend, NASAA and its member state agencies have attempted to secure federal and state statutes or regulations which will ensure voluntariness in the arbitration agreement process. In December 1987, NASAA recommended that Congress require broker-dealers to negotiate arbitration agreements. Statement of James C. Meyer Before the Subcomm. on Telecommunications and Finance of House Comm. on Energy and Commerce (Dec. 16, 1987). This call was renewed in June 1988. 20 Sec. Reg. & L. Rep. (BNA) 850 (June 3, 1988). In September 1988, at the time, the Massachusetts Securities Division adopted the Rule challenged in the present case, NASAA reported that some 15 of its other members were considering the adoption of



similar regulations. 20 Sec. Reg. & L. Rep. (BNA) 1436 (Sept. 23, 1988).

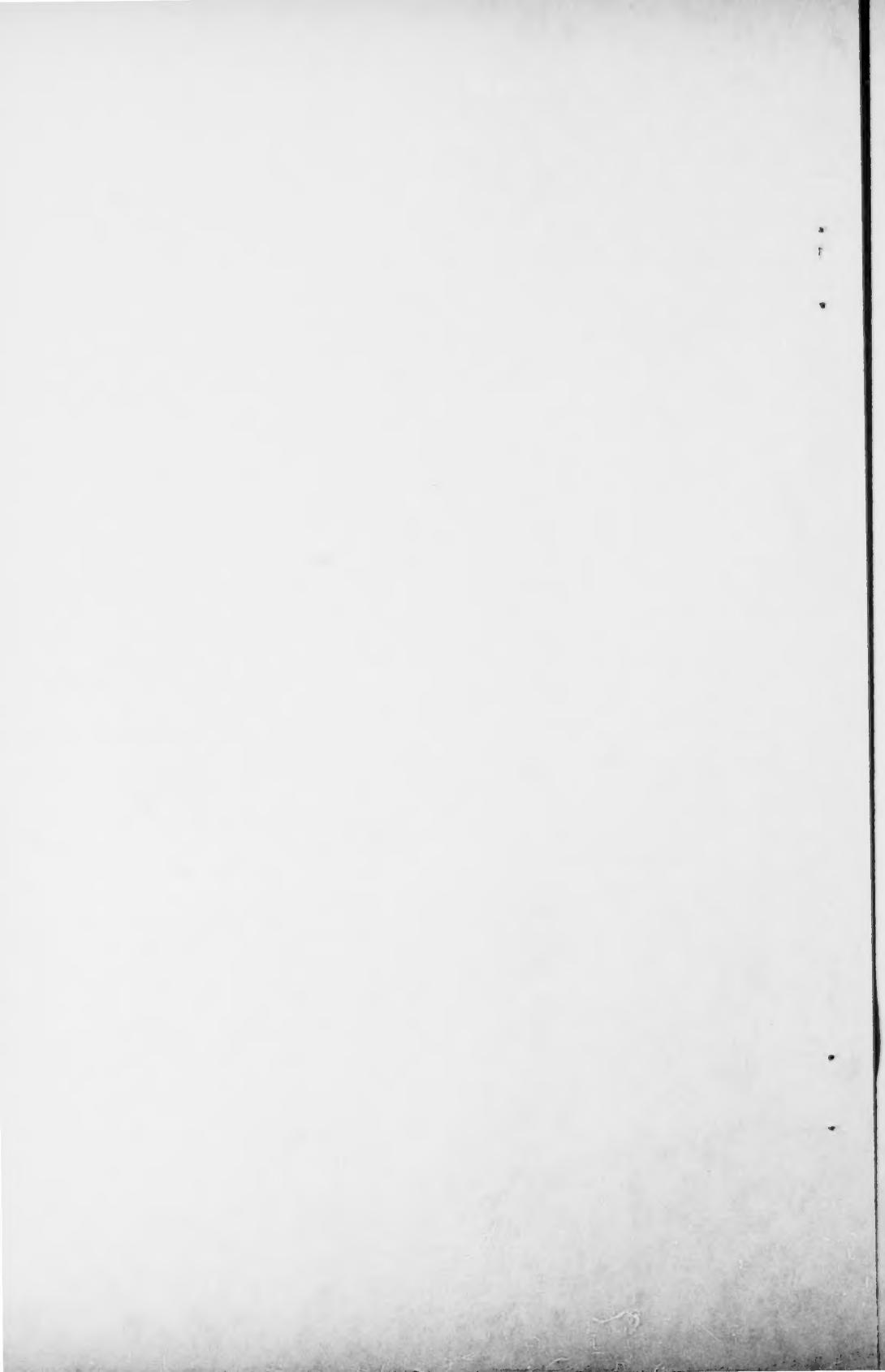
Nor is NASAA the only group concerned about the proliferation of the mandatory arbitration agreements in brokerage contracts through contracts of adhesion. As noted above at p.4, five state legislatures have considered bills which would prohibit brokerage contracts of adhesion requiring mandatory arbitration. As early as 1979, the SEC also became concerned about these contracts. In SEC Exchange Act Rel. No. 15984 (July 2, 1979), 17 SEC Docket 1167, the Commission recognized that arbitration clauses were "routinely required for margin accounts and often for cash accounts" The Commission went on to state: "Moreover, the customer may be precluded from doing business with the broker-dealer if he or she refuses to sign the agreement or the



broker-dealer is unwilling to accept any modifications of its terms." Id. at 1169.

More recently a study conducted by the SEC Staff lead the staff to recommend that the SEC initiate legislation to curb the use of these contracts of adhesion. See [1987-1988 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶84,241 (June 8, 1988). The Commission, however, refused to initiate such legislation or support HR 4960, 100th Cong. 2d Sess. (June 30, 1988), introduced by Representative Boucher, which would also outlaw such agreements. 20 Sec. Reg. & L. Rep. (BNA) 1054 (July 8, 1988).

The academic community is also concerned about the spread of these non-negotiable contracts of adhesion requiring arbitration in brokerage contracts. McCauliff and Tyms in their article New Protections in Arbitrating Public Securities Disputes in the Wake of McMahon: Foregone Conclusion or Will-O'-

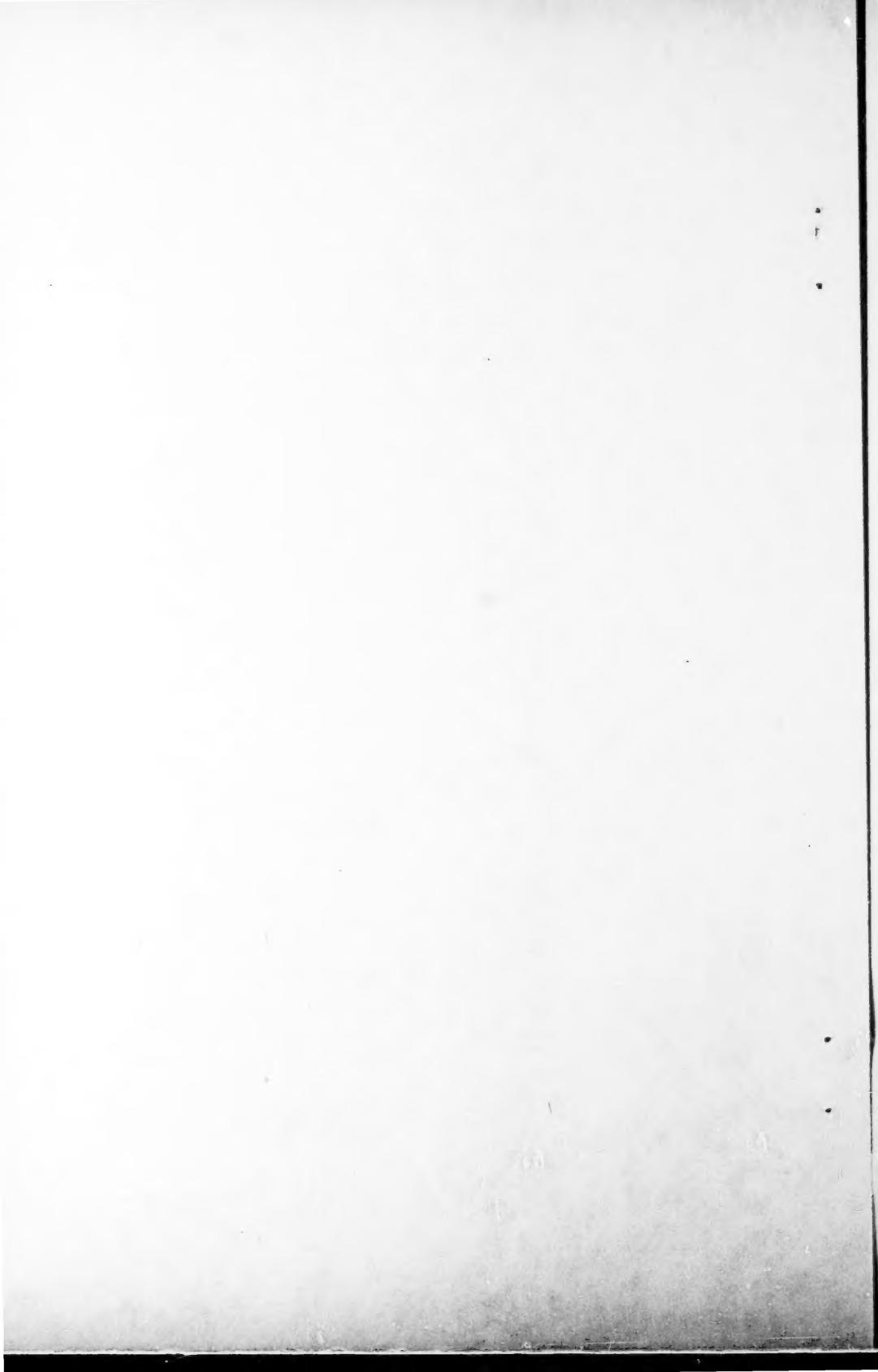


The Wisp?, 34 VILL. L. Rev. 25, 56 (1989)

said:

[Public confidence in the arbitration process] can only be earned by maintaining a de facto as well as a de jure image of fairness." The de facto image of fairness can be promoted by removing any appearance of adhesion contracts. A contract of adhesion arises when a party with superior bargaining power presents a standardized form contract to a party of lesser bargaining power whose choice is limited to accepting or rejecting the contract without opportunity to negotiate. While it is true that mere inequality in bargaining power does not make a contract unenforceable, nonetheless, when the arbitration agreement is presented as a precondition to opening an account, the image of de facto fairness is seriously compromised. Therefore, it should be clear to the investor that the agreement is entirely optional.

[Footnotes omitted.] See also DiFiore, Problems in Alternative Dispute Resolution: Arbitration Agreements as Contracts of Adhesion in Consumer Securities Disputes, 90 Commercial L.J. 259 (1988); Katsoris, The Arbitration of A



Public Securities Dispute, 53 Fordham L. Rev. 279 (1984).

Nor is the concern of NASAA limited to mandatory arbitration contracts in the brokerage area. NASAA members are increasingly seeing private placement memoranda for offering sold under the securities registration exemptive provisions of both the state and federal securities acts which contain mandatory predispute arbitration agreements. Again, these offering are being made on a take-it-or-leave-it basis with the purchaser having no opportunity to reject the arbitration clause. Unlike brokerage agreements which this Court in McMahon held could be supervised by The SEC under Section 19 of the Exchange Act of 1934, 15 U.S.C. §78s, these mandatory arbitration agreements are not subject to direct SEC control or do not have to call for arbitration in a system subject to SEC



control. Thus the investor, if he wishes to invest in these products, has no choice but to agree to arbitrate, possibly in a forum which is not subject to regulation by the SEC. If the present case is allowed to stand, the states will be powerless to protect investors from such overreaching. Southland Corp. v. Keating, 465 U.S. 1 (1984).

Thus, there is wide support for the curbing of contracts of adhesion which require mandatory arbitration in the securities area. However, the ability to implement these reforms at the state level is left in question by the First Circuit's decision in the present case. While the decision is not binding outside that Circuit, and some agencies and legislatures appear willing to push ahead with Rule or statutes similar to the Massachusetts Rule declared preempted, it would be better if the issue was finally



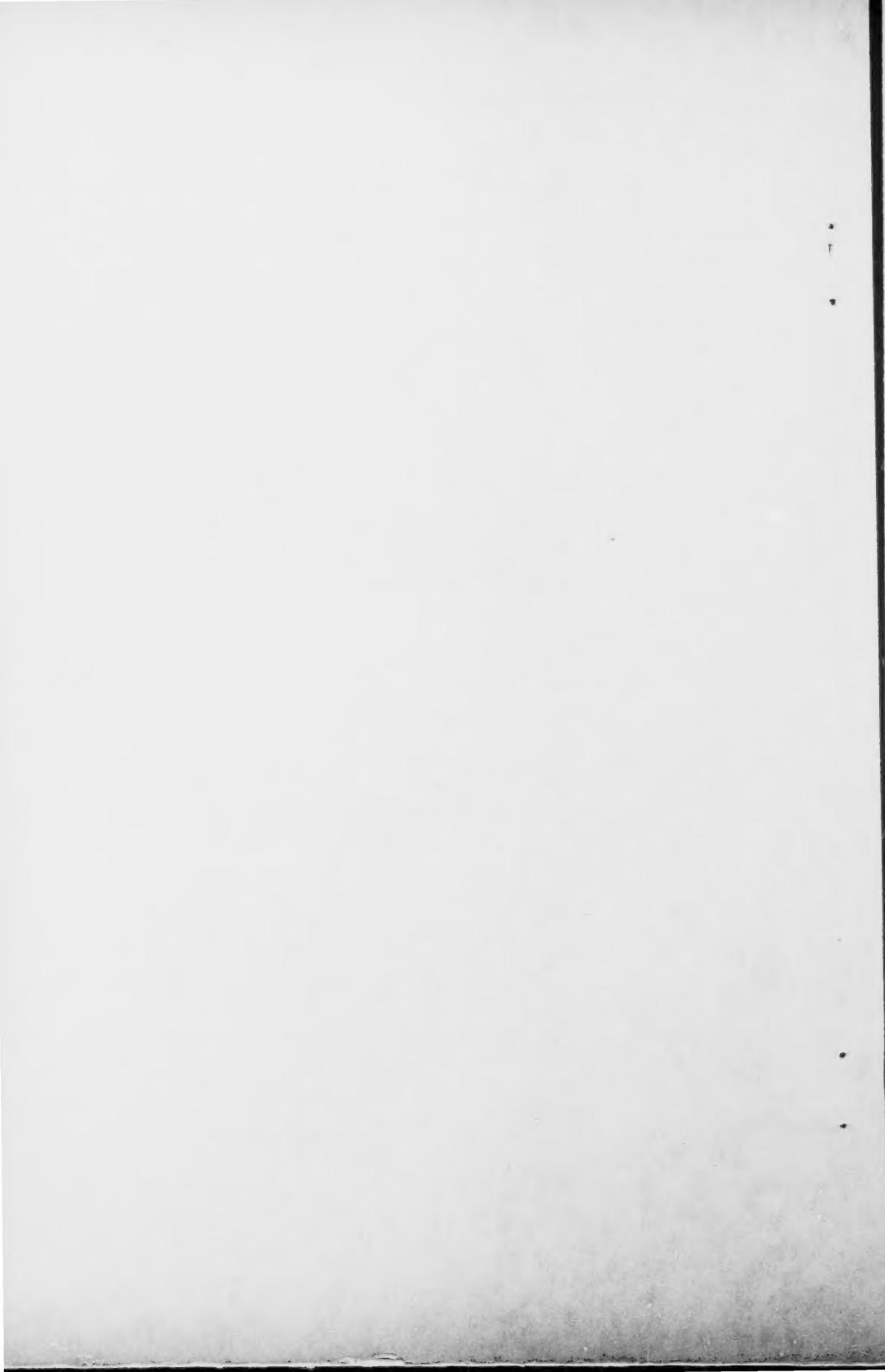
resolved by this Court. Therefore, NASAA urges this Court, on the basis of the public interest in this issue as outlined above, to grant certiorari and finally resolve the dispute.

III. THE COURT SHOULD GRANT CERTIORARI BECAUSE THE PRESENT CASE HAS WIDE INTEREST BEYOND THE SECURITIES AREA.

Following Chief Justice Taft's criteria, the Court should grant certiorari in the present case because it has wide interest beyond the securities field. Non-negotiable contracts of adhesion requiring predispute consent to arbitrate are proliferating in many areas other than securities. The Commonwealth identified a number of these areas in Point II of their brief. NASAA's research has identified a number of others.



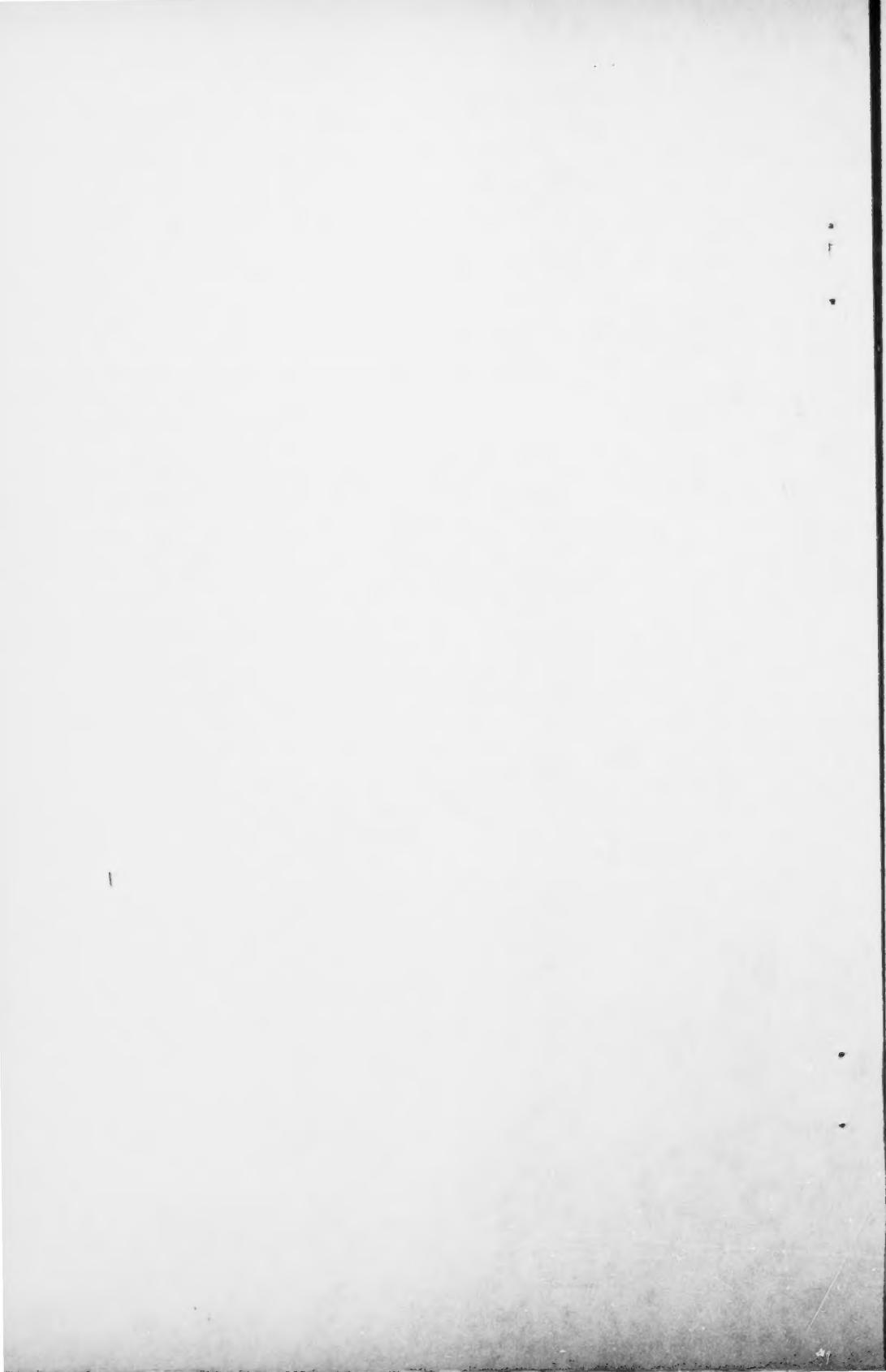
The Commonwealth pointed out that the Bank of America and Marathon National Bank of Los Angeles are extensively using non-negotiable arbitration clauses in a wide variety of situations. The text of the Bank of America General Arbitration Clause and the one used in its Safety Deposit Agreements are reprinted in the Appendix to Comment, Lender Liability and Arbitration: Preserving the Fabric of Relationship, 42 Vand. L. Rev. 947, 981 (1989). This article indicates that the Bank of California is also extensively using such clauses and reports the text of that Bank's clause. Id. at 982-983. The article also points out the advantages to banks of the wide-spread use of such clauses as an aid in the control of lender liability in commercial lender situations. Use of such clauses in lender situations as a means to control "excessive lender liability judgments" was



advocated by James Pitts in Pitts,  
Arbitrating Lender Liability Claims, 106  
Bank. L.J. 227 (1989).

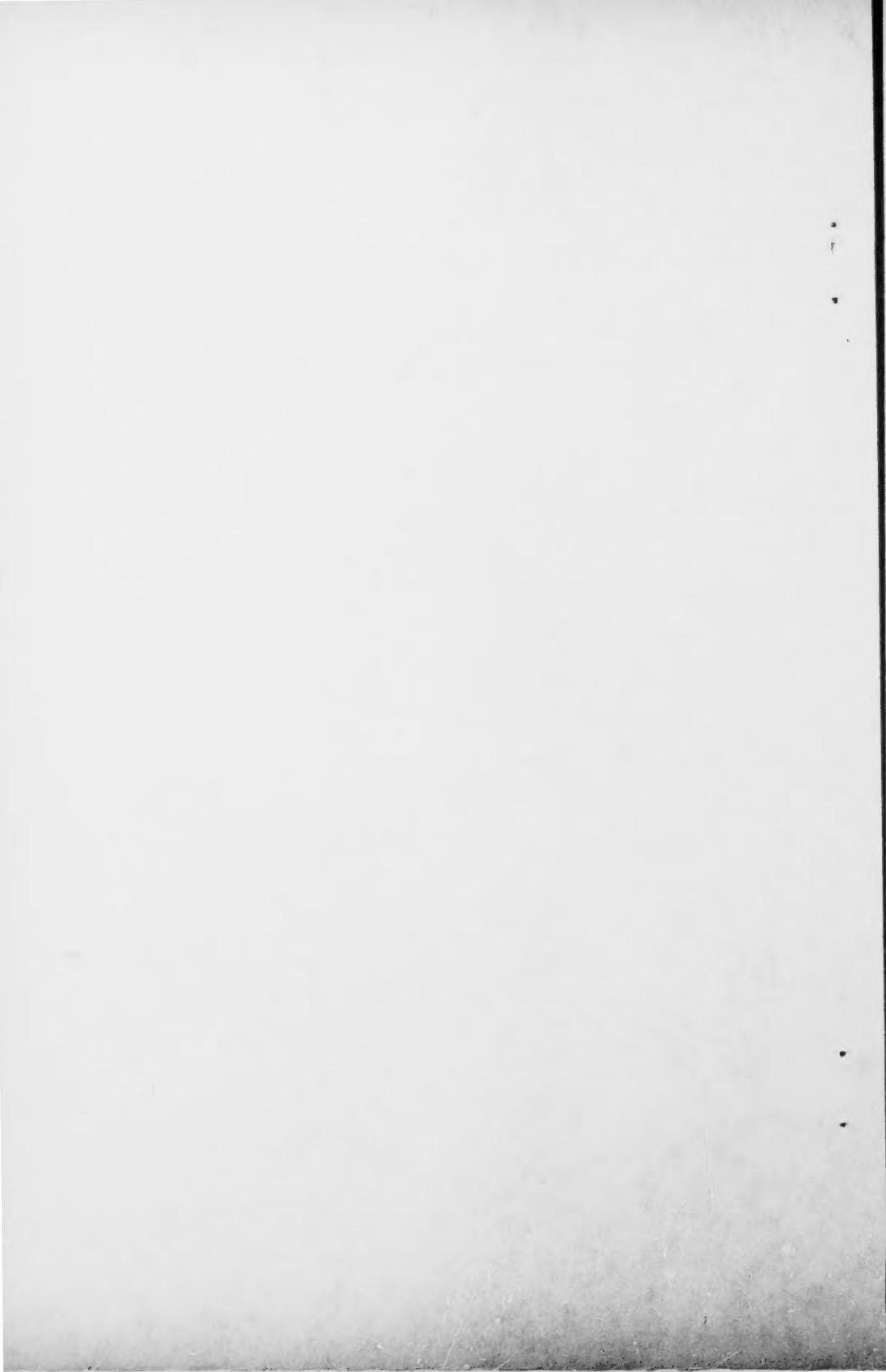
Such non-negotiable clause are appearing more frequently in the insurance areas. The Commonwealth pointed out their use in the malpractice and health care area. NASAA's research shows that such clauses are also being used in insurance re-insurance contracts, see Spotlight Report, Business Insurance 72, 74 (Nov. 6, 1989) (avail. on Nexis), and by State Farm, one of the largest retail insurance companies, in connection with its uninsured motorists coverage. Chicago Tribune, Chicagoland Section, p.2 (Sept. 19, 1989)(avail. on Nexis).

Finally, the Commonwealth noted the use of these agreements in connection with disputes between the automobile manufacturer and their dealers. In contrast to the decision by the First



Circuit in the present case, the court in Saturn Distribution Corp. v. Williams, Commissioner of the Department of Motor Vehicles of Virginia, 717 F. Supp. 1147 (E.D. Va. 1989), appeal pending Doc. No. 89-2773 (4th Cir.) (oral argument heard Dec. 6, 1989); upheld the authority of the Commissioner to restrict the use of such clauses. NASAA has discovered that these clauses are also being used in connection with disputes between the automobile dealers and their retail customers. Ex Parte Warren, 548 So.2d 157 (Ala. 1989), cert. filed, Doc. No. 89-567, 58 U.S.L.W. 3291 (Oct. 4, 1989).

The First Circuit decision in the present case was extremely broad. In essence, it held that the states could not adopt any statutes or regulation affecting the use of arbitration clauses unless such legislation or rules applied to contracts generally. Thus, the state could not



adopt limiting rules or legislation which was industry specific such as securities, banking, or insurance. If this decision is allowed to stand and followed by the other Courts of Appeal, it will have an extremely limiting effect on the ability of the states to protect their citizens from abusive arbitration practices in such traditional consumer protection areas as consumer credit, truth-in-lending, and automobile lemon laws. See Motor Vehicle Manufacturers Ass'n v. Abrams, 697 F. Supp. 726 (S.D.N.Y. 1988).

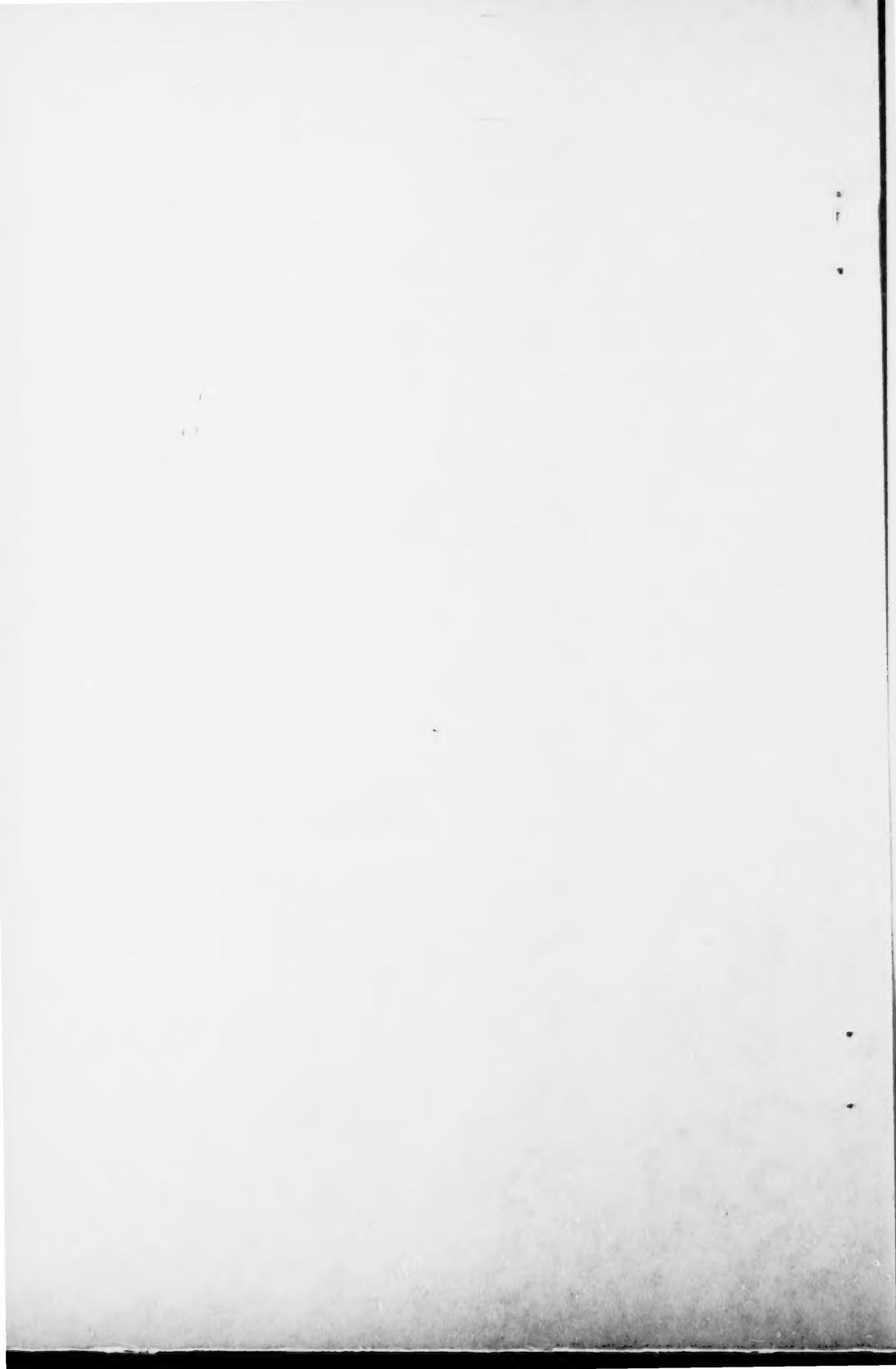
Concern about the extraordinary breadth of the First Circuit's decision in the present case and its application to areas beyond the securities area into other areas traditionally considered within the police powers of the states, NASAA understands has caused the Attorney General of Virginia to file a brief in support of the granting of certiorari in



the present case. It is NASAA's further understanding twenty-seven other state Attorney Generals joined in the filing of this brief. The fact of its filing and the support by the large number of other state attorneys general indicate the wide spread interest by the states and their regulatory agencies outside the securities area in the present case. NASAA joins with the state attorney generals in urging the Court to grant certiorari in the present case because of this wide spread interest it has generated in other areas of state regulation beyond securities.

IV. THE COURT SHOULD GRANT CERTIORARI IN THE PRESENT CASE BECAUSE THERE IS A POTENTIAL CONFLICT OF INTEREST BETWEEN THE CIRCUITS.

Another traditional test used by the Court to determine whether to grant certiorari is whether there is a conflict



among the circuits on the issue presented. To date, NASAA is aware of only two cases which have considered the power of the states to regulate or control the use of non-negotiable contracts of adhesion requiring mandatory arbitration. They have reached opposite results. The First Circuit's decision in the present case held that the states could not adopt such statutes or regulations unless that applied to all contracts generally. The decision by the district court in Saturn Distribution corp. v. Williams, Commissioner of the Department of Motor Vehicles of Virginia, 717 F. Supp. 1147 (E.D.Va. 1989), appeal pending, was that such regulation was not preempted by the Federal Arbitration Act. Thus there is a potential conflict between the circuits on the issue which this Court should resolve.



V. THE COURT SHOULD GRANT CERTIORARI IN THE PRESENT CASE BECAUSE THE FIRST CIRCUIT MISCONSTRUED THE PURPOSES AND OBJECTIVES OF THE FAA.

Finally the Court should grant certiorari because the First Circuit misconstrued the purposes and objectives of the Federal Arbitration Act in two very important ways. First, the First Circuit ignored the clear legislative history that the FAA was intended to apply only to voluntary agreements to arbitrate and was specifically not intended to cover contracts of adhesion. Second, the First Circuit also failed to recognize that state law governs the contracting process by which an agreement to arbitrate is formed and that the states have traditionally had the power to refuse to enforce unconscionable contracts.

The legislative history of the FAA

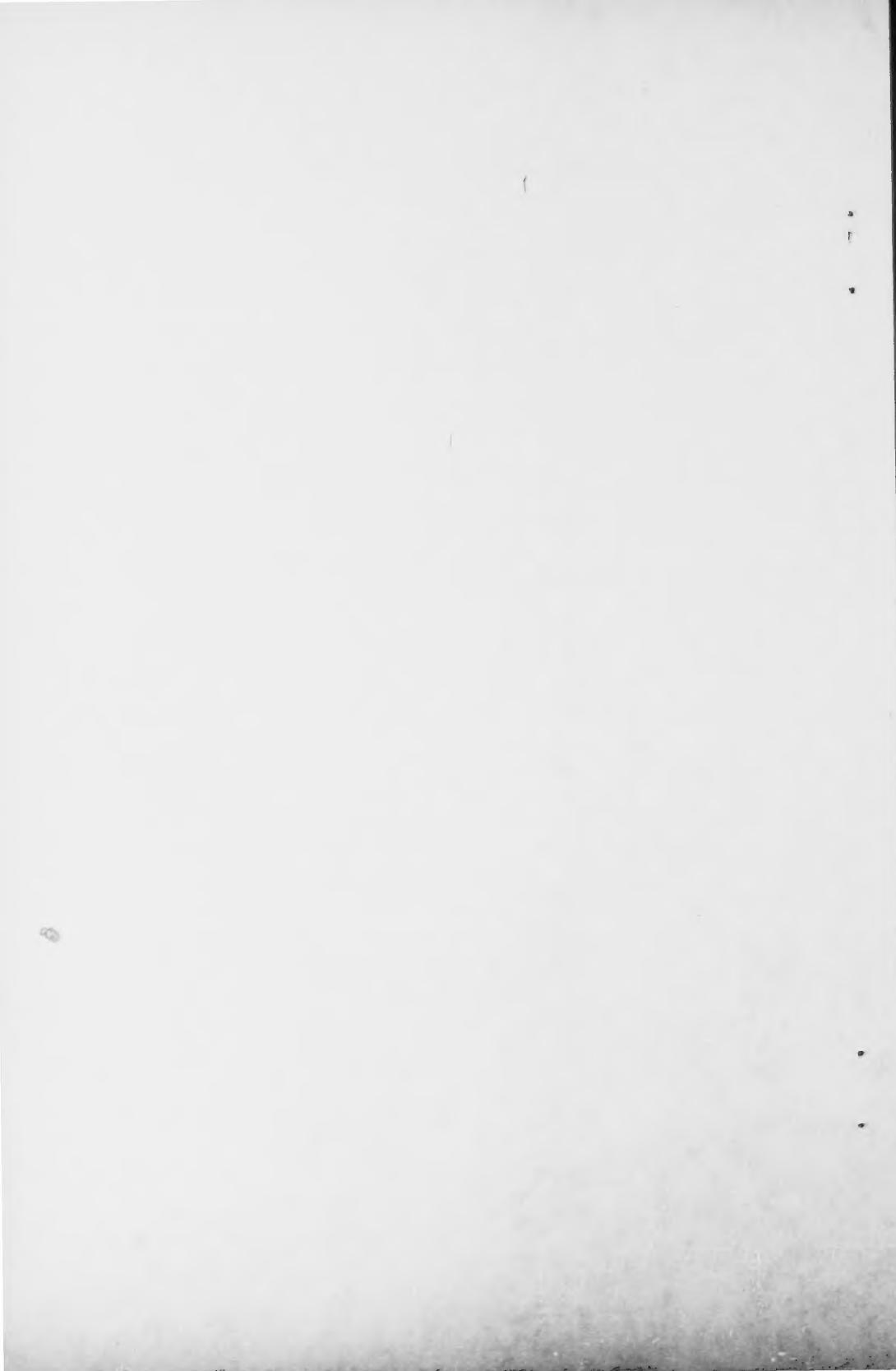


makes clear that it is intended to apply only to voluntary agreements to arbitrate:

The record... shows only the great value of voluntary arbitrations but the practical justice in the enforced arbitration of disputes where written agreements for that purpose have been voluntarily and solemnly entered into.

S. Rep. No. 536, 68th Cong., 1st Sess. at 3. [Emphasis added.] This Court has on numerous occasions recognized this principle. Most recently the Court said in Volt Information Sciences, Inc. v. Board of Trustees of Leland Stanford Junior University, \_\_\_ U.S. \_\_\_, 109 S.Ct. 1248, 1256 (1989), that "Arbitration under the Act is a matter of consent, not coercion."

More specifically, during the hearings leading to the adoption of the Act, the question was raised by Senator Walsh as to the intent of the Act to cover arbitration in those situations where the agreement to arbitrate was a product of a



non-negotiable contract of adhesion.

Senator Walsh said:

The trouble about the matter is that a great many of these contracts that are entered into are not really voluntarily [sic] things at all. Take an insurance policy: there is blank in it. You can take that or you can leave it. The agent has no power at all to decide it. Either you can make that contract or you can not make any contract. It is the same with a good many contracts of employment. A man says: "These are our terms. All right, take it or leave it." Well, there is nothing for the man to do except sign it; and then he surrenders his right to have his case tried by the court, and has to have it tried before a tribunal in which he has no confidence at all.

Hearing on S. 4213 and S. 4214 before the Subcommittee of the Judiciary, 67th Cong., 4th Sess. at 9 (1923). Senator Walsh went on to ask similar questions concerning contracts of adhesion in the shipping and construction industries. Id. at 10-11. In all cases, the proponents of the bill indicated that they did not intend the bill to cover such contracts.



This legislative history was recognized and accepted by three members of this Court in Prima Paint Corp. v. Flood & Conklin Mfg., 388 U.S.395 (1967). Justice Black speaking for the three in dissent said:

Senator Walsh cited insurance, employment construction and shipping contracts as routinely containing arbitration clauses and being offered on a take-it-or-leave it basis to captive customers or employees. He noted that such contracts "are really not voluntary things at all." because "there is nothing for the man to do except to sign it; and then he surrenders his right to have his case tried by the court...." He was emphatically assured by the supports of the bill that it was not their intention to cover such cases.

Id. at 414. (Black, J. dissenting)

[Emphasis added.]

Second, it has long been held that state, not federal, law controls as to whether the parties have entered into a binding contract to arbitrate. EASSA Properties v. Shearson Lehman Bros., Inc.,



852 F.2d 1301, 1304 n.7 (11th Cir. 1988); Supak & Sons Mfg. Co. v. Pervel Indus. Inc., 593 F.2d 135, 137 (4th Cir. 1979); Cook Chocolate Co. v. Salomon, Inc., 684 F. Supp. 1177 (S.D.N.Y. 1988); Rush v. Oppenheimer, 681 F. Supp. 1045 (S.D.N.Y. 1988); Graniteville Co. v. Star Knits of Calif. Inc., 680 F. Supp. 587 (S.D.N.Y. 1988). Cf. Perry v. Thomas, 482 U.S. 483, 492 n.9 (1987). This conclusion is consistent with the opinion expressed by the proponents of the FAA as expressed in a 1925 article written immediately following the passage of the Act. They said:

It is no infringement upon the right of each State to decide for itself what contracts shall or shall not exist under its laws. To be sure whether or not a contract exists is a question of the substantive law of the jurisdiction wherein the contract was made.

Committee of Commerce, Trade & Commercial Law, The United States Arbitration Law and



Its Application, 11 ABA J. 153, 154 (1925).

NASAA submits that the same should be true under that portion of Section 2 of the Act which provides that arbitration agreements "shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract." 9 U.S.C §2. [Emphasis Added.] This Court in Shearson/American Express Co. v. McMahon, 482 U.S. 220, 226, 230 (1987), recognized that excessive economic power would provide a basis for voiding an arbitration agreement under ordinary principles of contract law under Section 2. See also, Katsoris, The Arbitration of A Public Securities Dispute, 53 Fordham L. Rev. 279, 307 (1984). Such contract would be unconscionable.

The determination of excessive economic power or unconscionability, however,



should be a matter of state, not federal, law. Further, a finding of such unconscionability can be made through legislative or administrative rule-making process as well as by court decision. The findings of the Secretary in adopting the Rule in the present case amounted to a finding of unconscionability. Such conclusion finds support in the academic literature, see e.g., DiFiore, Problems in Alternative Dispute Resolution: Arbitration Agreements as Contracts of Adhesion in Consumer Securities Disputes, 93 Commercial L.J. 259 (1988), and should have been respected by the First Circuit.

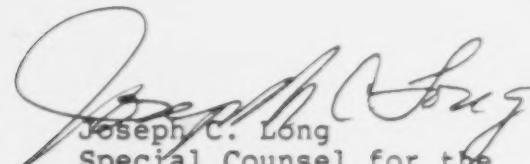
#### CONCLUSION

For the reasons set forth above and those outlined in the brief of the Commonwealth, NASAA joins with the Commonwealth in urging the Court to grant



the petition for writ of certiorari and  
hear the case on its full merits.

Respectfully submitted,

  
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